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SUBJECT: RUSSIA AND CHINA CONTINUE QUIET ENGAGEMENT

¶1. (SBU) In contrast to the high-profile visit of President Obama to Moscow two weeks ago and the attendant expectations for a "reset" U.S.-Russian bilateral relationship, Chinese President Hu Jintao's June 16-18 official visit was low key and almost routine. Moscow and Beijing are continuing a quiet engagement of strategic partnership, one characterized by similar views on major regional issues such as North Korea and Afghanistan, as well as coordination of positions in international organizations. While the two countries enjoy a healthy trade relationship, China clearly is the lead economy of the two with more investment power and a bigger appetite for consumption. Moscow's resentment that the bilateral trade consists of Russia trading its raw material for finished Chinese goods and Beijing's frustration at the investment barriers in the Russian economy are potential sources of friction. While Russian officials at the federal level uniformly downplay migration issues as a problem, regional officials and the public continue to exhibit occasionally a xenophobic fear that the much larger Chinese population across the border would one day overwhelm the smaller Russian population and exert control over Russian economy and society through its migrants.

China and Russia on Equal Political Footing

¶2. (SBU) That Russia and China were the two main driving forces behind the Shanghai Cooperation Organization (SCO) and continued to find significant value in their "strategic partnership" was driven home when, on the heels of the June 15-16 SCO summit and the first ever BRIC summit in Yekaterinburg, Chinese President Hu Jintao traveled to Moscow June 16-18 for an official visit. There, he met with President Medvedev, Prime Minister Putin and the Speaker of the State Duma Boris Gryzlov to discuss a range of political and economic issues, including security and stability in Central Asia, SCO's role in tackling terrorism, and the drug trade originating from Afghanistan. Both MFA officials and the Russian media noted that following last year's demarcation of the Russian-Chinese border, which put an end to a long-standing dispute between the two neighbors, the slate of outstanding issues was completely clean and there was no longer any political obstacle standing in the way of a continued deepening of the bilateral relationship.

¶3. (SBU) In particular, Moscow and Beijing demonstrated anew their similar outlook on a number of regional issues during Hu's two-day visit. Releasing a joint statement June 17 on a wide range of political, economic, domestic and international issues, Medvedev and Hu reaffirmed Russia and China's support of the UN Security Council's actions following North Korea's May 25 nuclear test and other provocations, and agreed that Iran's nuclear program should strictly have peaceful civilian energy ends. While calling on Pyongyang to return to the Six Party Talks, the joint statement also warned the countries in the region to refrain from an arms race. It reflected both Moscow and Beijing's unique positions as friends of Pyongyang, as well as their shared unease that a deterioration of the security situation in Northeast Asia would lead to either a

rearmed Japan or a deepening of the U.S.-Japanese-South Korean alliances to the detriment of Russia and China's long term national interests.

14. (SBU) On Afghanistan, the Chinese embassy here told us that Beijing has been watching very closely the increasing cooperation between the U.S. and Russia, and hoped to use the terms of the just concluded lethal transit agreement as a guide for its own deliberations on the U.S. request to use Chinese territory and space for the transit of ISAF supplies.

Beijing Clearly Leads on Economic Issues

15. (SBU) MFA contacts pointed to the serious discussion of the global financial crisis, reform of the international financial institutions, and the role of BRIC during Hu's official visit as evidence of a healthy economic dialogue between two important economies. Some of them also admit, however, that Moscow does not have the capacity as Beijing does to help turn the crisis situation around. While Russia has offered loans and assistance to former Soviet republics and has indeed delivered on some of them (most notably to Kyrgyzstan, Armenia and Belarus), the scope of such assistance cannot compete with the USD 10 billion line of credit that Beijing announced it would offer for SCO development projects during the Yekaterinburg summit. More notably, instead of the new SCO Presidency Uzbekistan, Beijing will host in October the SCO Prime Ministers' meeting, and Russian officials describe this upcoming meeting as the economic highlight of the year for the SCO, where China is expected to provide in more detail the terms of its USD 10 billion offer.

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16. (SBU) On the bilateral front, Moscow and Beijing signed a series of agreements, including: two memorandums of understanding (MOU) on gas and coal cooperation, an MOU between the Russian Ministry of Economic Development and the Chinese Ministry of Commerce on the promotion of bilateral trade and exchange of technical goods and machinery, an agreement for a USD 700 million dollar credit from the Chinese Export-Import Bank to the Russian Development Bank (VEB), and an MOU between Russian investment and asset management company The Renova Group and China's state gold-prospecting corporation National Gold Group Corporation (CNGGC) to cooperate in gold and platinum exploration and mining in the Kamchatka Peninsula. The two leaders also discussed electric and atomic energy cooperation, and the use of national currencies in energy trading. Separately, Russian company Lukoil and its Chinese counterpart Sinopec signed a contract to supply three million tons of crude oil from the South Hylchuyu deposits in Nenets Autonomous Region to China.

17. (SBU) MFA officials told us that Russia's growing energy cooperation with China is part of an effort to diversify its energy export markets, particularly in light of recent energy discords involving Europe and problematic transit issues with neighboring states. In continuing to focus on energy deals as the only economic deliverables of substance, however, Moscow is perpetuating the qualitative imbalance in the Russian-Chinese bilateral trade, of which the GOR has long complained. The lack of a manufacturing base is hampering the export of finished goods from Russia, experts tell us, and in the absence of meaningful plans to invest in its industrial infrastructure and encourage small and medium business development in favor of the large state-owned and oligarch companies with loose Kremlin ties, the typical Russian business only knows how to conclude deals to sell Russia's abundant natural resources.

18. (SBU) Another notable issue in the economic relationship is the lack of mutual investment. Though trade between Russia and China totaled USD 56 billion last year, the cumulative investment from China to Russia is only USD 1.7 billion, and from Russia to China a paltry USD 400 million. While Russian and Chinese leaders discuss means to expand mutual investment, our Chinese embassy contacts complain to us that Russia still has many legal, administrative, and procedural barriers that hinder investment, particularly with regard to strategic sectors in which China has expressed interest in

investing.

Russians and Chinese Play Down Migrant Problem

¶9. (SBU) Officially, both Russian and Chinese officials played down migration as a problem between the two countries, even though it does occasionally feature in summit discussions, including during Hu's June visit. Indeed, experts agree that the transient nature of the Chinese migrant workers and their overwhelming preference to return home after a four to five period of working in Russia make this issue a tempest in a teapot. In the Russian Far East, scholars such as Viktor Larin of the Institute of History, Archaeology and Ethnology of the Peoples of the Far East believe the number of Chinese residents there is closer to the 30,000 to 40,000 range than the 100,000 number that is widely quoted in the press, accounting for only two percent of the RFE economy.

¶9. (SBU) Unofficially, officials outside foreign policy circles and in the regions, as well as local trade unions and the public, continue to be wary of the possibility of a large influx of Chinese nationals into Russia, especially during the current economic downturn. Spotty statistics on the relatively low number of Chinese in Russia are no match against public apprehension that only 6.7 million people, with the population steadily dwindling, live in the enormous Far East region, while at least 100 million Chinese inhabit lands directly adjacent to Russia on the other side of the border. China's voracious appetite for Russian raw materials and the presence of Chinese industrial and mining companies in the Far East, bringing with them seemingly large numbers of Chinese workers, add to the Russian public's unease and some officials' concern that the inflow of Chinese workers represented a "very dangerous trend."

¶10. (SBU) There are recent signs that migration may become a more serious issue in Russian-Chinese relations after all. Last month, as Russian authorities closed down Moscow's sprawling Cherkizovskiy market (septel) directly adjacent to the more famous Izmailovo market, purportedly a crackdown on trade, sanitation, and fire code violations, the Chinese government expressed concern over the welfare of Chinese citizens affected by the closure and an estimated USD 2 billion in merchandise that was seized. As in most such cases, statistics regarding the migrants working at the market varied widely. While groups such as the Federation of Migrants of Russia estimated that the market employed approximately 100,000 workers, some 45,000 of them migrants, the Federal Migration Service states that only 3,000 migrants worked at Cherkizovskiy out of a

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total of 14,000 workers. Regardless of the numbers, the July 22 arrival in Moscow of a Chinese delegation led by Deputy Commerce Minister Gao Hucheng to discuss with the Russian authorities ways to recover the seized merchandise and help the traders to relocate their shops is an indication of the seriousness with which the Chinese government is taking this issue.

BEYRLE